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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of In the Matter of Petition of WorldCom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc., and for Expedited Arbitration	))))))))))	CC Docket No. 00-218
In the Matter of Petition of AT&T Communications of Virginia, Inc., Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc., and for Expedited Arbitration	))))))))))	CC Docket No. 00-251

DECLARATION OF PATRICK A. GARZILLO

1. My name is Patrick A. Garzillo. My business address is 1095 Avenue of the Americas, New York, New York. I am the Vice President of Service Costs in the Finance Department at Verizon. The Service Cost organization is responsible for developing costs for services provided by Verizon. As Vice President, I am responsible for managing and supervising the development, preparation and analysis of service cost studies for retail and wholesale products and services, separations, and part 64/cost allocations in all of Verizon's serving areas.

2. I have over 30 years of experience with Verizon and its predecessor companies. During this time, I have held a variety of positions of increasing responsibility in various internal functional organizations, including Network

Engineering, Service Costs, Carrier Access Services, Special Services Operations, Retail Product Management and Market Management, and Wholesale Market Development for Competitive Local Exchange Carriers.

3. I hold a Bachelor of Science degree in Electrical Engineering Technology from the New York Institute of Technology, which I earned in 1969, and a Masters of Science degree in Management Science from Polytechnic University, which I earned in 1975. In addition over the past several years I have attended business and educational seminars at Duke University's Fuqua School of Business, University of Pennsylvania's Wharton School of Business, Brookings Institute and Columbia University.

4. The purpose of my declaration is to describe the immediate, irreparable financial harm to Verizon that would result from both the policy decisions and the rate decisions in the Memorandum Opinion and Order released August 29, 2003 ("*Order*") in this proceeding. In particular, the *Order* will produce dramatically reduced rates for the unbundled network element platform ("UNE-P") and for high capacity loops that will be among the lowest rates in any of Verizon's service areas. These rates will be well below the current Virginia rates that the Commission has already found to be TELRIC compliant, and that have already caused competitors to alter their focus from investment in their own facilities to heavy reliance on the UNE platform. The *Order* will also create new subsidies and exacerbate existing subsidies that will further undermine incentives for carriers to invest in their own networks. And it will accelerate the dramatic growth in the UNE platform and the conversion of special access circuits to enhanced extended links, or "EELs." As a result, both Verizon and the public interest will suffer irreparable harm if the *Order* is allowed to go into effect.

5. History of Virginia TELRIC Rates. In 1999, the Virginia State Corporation Commission ("SCC") adopted rates for unbundled network elements using the TELRIC methodology. *See Ex Parte: To Determine Prices Bell Atlantic-Virginia, Inc. is Authorized to Charge Competitive Local Exchange Carriers in Accordance with the Telecommunications Act of 1996 and Applicable State Law,* Case No. PUC970005, Final Order (Apr. 15, 1999) ("*Final Order*"). The rates set in the Virginia SCC's Final Order included all of the key rates such as the loop, switching, port, and transport rates. The Virginia SCC found that these rates complied with TELRIC. There were some UNEs, however, that were not included in the *Final Order* (for example, the UNEs established in the FCC's *UNE Remand Order* which was released after the SCC completed its TELRIC proceeding.).

6. Later in 1999, the Virginia SCC issued a series of orders in which it explained that it would no longer conduct arbitrations pursuant to Section 252 of the Telecommunications Act, and directed parties to consult the FCC for resolution of issues raised in interconnection negotiations. *See Petition of Cavalier Telephone, LLC For Arbitration of Interconnection Rates, Terms and Conditions and Related Relief,* Case No. PUC990101, Order (June 15, 2000); *Petition of Cox Virginia Telcom, Inc. v. Verizon Virginia, Inc., For Declaratory Judgment and Conditional Petition for Arbitration of Unresolved Issues,* Case No. PUC000212, Order on Dismissal (Nov. 1, 2000).

7. As a result, Verizon VA determined rates for UNEs that were not included in the Virginia SCC's *Final Order* in one of three ways. First, for those UNEs that had an existing UNE rate element comparable to one that had been set by the Virginia SCC in the *Final Order*, Verizon VA charged the rate set by the Virginia SCC, as long as that

existing rate was lower than or equal to the rate any Virginia CLEC was then paying under an interconnection agreement. Second, for those UNEs that did not have an existing comparable UNE rate set by the SCC, Verizon VA charged the lower of (1) the comparable New York rate adjusted to reflect differences in costs between New York and Virginia; or (2) any lower rate that a CLEC was then paying Verizon under the terms of an existing interconnection agreement. Third, some rates were adopted from New York without adjustment. These included rates, such as non-recurring rates, for which the Commission's Universal Service Model did not provide a comparison of relative cost levels.

8. In connection with its application to provide in-region interLATA services in Virginia, the per minute originating and terminating unbundled switching rates previously set by the Virginia SCC were reduced by 36 percent following discussions with this Commission's staff in order to meet the so-called benchmark standard applied by this Commission in reviewing applications under section 271. Specifically, the switching rates were reduced to meet the benchmark standard compared to New York. The loop rates previously set by the Virginia SCC already satisfied a benchmark comparison to New York loop rates. In fact, the loop rates in Virginia were *lower* than the benchmarked New York loop rates. The net effect of the change in switching rates, therefore, was to reduce the UNE-P rate in Virginia to a level that was even *lower* than in New York in order to satisfy this Commission's benchmark standard. In its October 30, 2002 order approving Verizon's long distance application for Virginia, the Commission found that all of Verizon VA's UNE rates complied with its TELRIC pricing rules. *Virginia 271 Order* ¶ 86.

9. The Commission's finding that Verizon's rates complied with TELRIC also included Verizon VA's unbundled DS1 and DS3 loop rates. *See id.* The Virginia SCC had determined TELRIC rates for unbundled DS1 loops in the *Final Order*. The statewide average DS1 loop rate was lower than the benchmark comparison rate for New York. Because the Virginia SCC had not set a TELRIC rate for unbundled DS3 loops, Verizon VA used the cost-adjusted New York rate for unbundled DS3 loops in Virginia. In addition, the monthly DS3 rate in New York includes not only a fixed component but a per quarter mile charge. In Virginia, the rate structure did not include a per quarter mile charge. Consequently, Verizon VA incorporated the per quarter mile rate element into the fixed rate element.

10. <u>The August 29 Pricing Order</u>. The *Order* in this proceeding establishes new recurring rates for unbundled loops for Verizon VA. With respect to other rates, the *Order* makes a number of decisions on both policy (for example, rate structure) and rate issues (such as specific cost inputs) and requires the parties to resubmit their cost studies after having reflected the policy and rate decisions in the models the *Order* adopts. Verizon VA is in the process of preparing its compliance filing and therefore does not yet have final rates, but it has made estimates of the rates likely to be produced when the cost models are run with the changes required by the *Order*. Among other things, as discussed in more detail below, the *Order* will result in switching rates that are *60 percent* lower than the current switching rates that were already reduced in connection with Verizon's long distance application for Virginia, and establishes high capacity loop rates that are *half* of current rates that benchmark to New York. *See* Attachment 1. The

rates that will result from the *Order's* decisions will cause severe and irreparable financial harm to Verizon VA if the order is allowed to take effect.

11. *Loops.* The *Order* produces a statewide average loop rate (for 2-wire basic loops) that is marginally higher than the previous Virginia statewide average loop rate -- $14.43 compared to $13.76. Although the *Order* increases the statewide average loop rate slightly (by $0.67), the new loop rates are still more than $1.00 *lower* than the equivalent rates in New York when the cost differences between the two states are taken into account. *See* Table below. In addition, rates for other types of loops have been reduced across the board; as I discuss further below in connection with rates for DS1 and DS3 loops, some of the rate reductions have been drastic.

State	Statewide Model Loop Cost	Statewide Average Loop Rate	Cost Ratio to New York	Rate Ratio to New York	(NY rate x 135%) - VA rate
NY	$10.37	$11.49	100%	100%	$15.51
VA	$13.96	$14.43	135%	126%	$14.43
					$ 1.08

12. *Switching.* The *Order* prescribes a drastic new rate structure for local switching that requires all end office local switching costs to be recovered through a flat-rate charge. None of the 31 state jurisdictions in which Verizon does business has imposed a similar rate structure for Verizon's local switching rates; instead, all have recognized that a significant portion of local switching costs are usage sensitive and have allowed them to be recovered through usage sensitive rates.

13. In addition, the *Order* prescribes the inputs to be used in setting these new flat-rated charges. As I noted above, Verizon VA is in the process of preparing its

compliance filing and therefore has not yet determined final switching costs, but it has made estimates of the rates likely to be produced when the cost models are run with the changes required by the *Order*. The effect of the *Order* will be to reduce the price of switching for the average user by nearly 60 percent. Indeed, the *Order* will produce rates for end office switching that are by far the lowest in effect in any of the 31 jurisdictions where Verizon provides local service. No party in this proceeding proposed switching rates as low as those that will result from the *Order's* decisions. In fact, the switching rates (plus other non-loop rates) will be *one-third* lower than what AT&T proposed in this proceeding and even lower than WorldCom's $2.94 flat-rate proposal. (Because AT&T agreed with Verizon that certain switching costs are usage sensitive, it did not propose a flat-rated switching charge. To make this comparison, therefore, Verizon calculated the average revenue per UNE-P line using AT&T's proposed loop and non-loop element rates and the same average minutes of use – based on Dial Equipment Minutes from ARMIS – that have previously been used in the Commission's benchmark calculations. Verizon then subtracted AT&T's proposed loop rate to get the equivalent non-loop cost.)

14. *UNE Platform*. As I described above, at the time the Commission approved Verizon's application to provide in-region interLATA service in Virginia, the non-loop rates met a benchmark comparison with New York and the loop rate was below the benchmark; as a result, the UNE platform in Virginia already costs more than $2.00 less per line than the equivalent cost-adjusted New York rate. Under the *Order*, the new UNE platform rate when compared to New York will be even lower – the small increase in the loop rate is more than offset by the new, much lower switching rate. As noted

above, unbundled switching rates will be slashed by nearly 60 percent, reducing the statewide UNE-P rate by nearly $3.00. In other words, the statewide UNE-P rate will now be *$5.00,* or more than 20 percent, below the cost-adjusted New York UNE-P rate. The combined effect of the *Order's* decisions on loop rates, switching, and the other elements that make up the UNE-P will produce a platform rate for residential users in Virginia's Density Cell 1 – which includes approximately 75 percent of Verizon VA's access lines – that is the second lowest set by any of Verizon's states for comparable density zones.

15. As noted above, moreover, the *Order* requires that end office switching be priced on a flat-rated basis, even though none of the state commissions in the 31 jurisdictions where Verizon provides local service has required Verizon to price unbundled switching on a flat-rated basis. Doing so means that customers with below-average usage levels will subsidize customers with above-average usage levels. CLECs typically target those high-usage customers. This means that Verizon, which must serve *all* customers, including the lowest-usage customers, will subsidize CLECs, which will now have even more incentive to rely on Verizon's network rather than investing in their own or alternative facilities. For example, based on the usage assumptions the Commission used in the Pennsylvania 271 proceeding, *Pennsylvania 271 Order,* ¶ 67, n. 252, which correspond to WorldCom's own numbers for for its customers' minutes of use,[1/] the platform rate in Virginia under the *Order* would be discounted more than 25

[1/] WorldCom, UNE-P Price Squeeze Prevents Robust Local Competition -- TELRIC Analysis at 21 (Oct. 2, 2000) (comparing switching rates among states assuming "1,200 originating local minutes and 1,200 terminating local minutes"), attached to Ex Parte Letter from Keith L. Seat, MCI, to Magalie R. Salas, FCC, CC Docket No. 00-176 (Oct. 3, 2000).

percent – or more than $6.00 – from the benchmark standard for the equivalent customer in New York.

16. *NRCs.* The *Order* requires that many non-recurring costs be recovered through recurring rates. In addition, the *Order* will likely produce rates that are far below those that the Commission determined were TELRIC compliant less than a year ago even where it still permits rates to be charged on a non-recurring basis. For example, the non-recurring charge for installing new service using an unbundled loop will be slashed more than 90 percent from $61.04 to less than $5.00. Even assuming that the $0.67 increase in the recurring loop rate is all intended to recover Verizon's non-recurring cost of installation, it would take nearly *seven years* (even without taking into account the time value of money) before Verizon could recover its non-recurring costs for this installation. Since WorldCom claims, and the Commission has accepted, that WorldCom loses half its customers in the first three *months*, *see Triennial Review Order* ¶ 471, it is obvious that the *Order's* recurring rates will not come close to allowing Verizon to recover its non-recurring costs. In addition, in the last seven years, more than 140 CLECs in Verizon's service areas have filed for bankruptcy. Of those, more than 50 have gone out of business. *See* Attachment 2. Again, it is clear that the *Order's* recurring rates will not come close to allowing Verizon to recover its non-recurring costs from carriers that go out of business during this period.

17. By definition, "non-recurring costs" are one-time expenses incurred by Verizon to provision or terminate a service or element for a CLEC. The *Order* therefore forces Verizon to act as a banker for the CLECs: Verizon must extend credit to individual CLECs for immediate cash outlays, but can recover that cost only through

periodic payments over time. As noted above, the problem is exacerbated by the fact that the CLECs' customers may disconnect, or the carriers themselves may go out of business, well before the non-recurring cost has been recovered in recurring rates. The *Order*, however, does not make any provision – either directly in the rate, in the general uncollectible rate allowed, or in the cost of capital – for the substantial added cost and risk that Verizon will incur under the *Order*.

18. *DS1 and DS3 Loops*. The *Order* slashes rates for unbundled DS1 and DS3 loops approximately in *half* from the levels that benchmark to New York and were deemed TELRIC-compliant less than a year ago, and in some cases by even more. *See* Table below. The new statewide average DS1 loop rate will be the lowest, and the DS3 loop rate will be second lowest set by a state commission for Verizon in any of the its 31 jurisdictions.

	VA Existing Rate	VA *Order* Rate
DS1		
Density Cell 1	$110.61	$51.13
Density Cell 2	$142.49	$65.62
Density Cell 3	$181.29	$122.25
Statewide Average	$119.15	$62.05
DS3		
Statewide	$1,181.15	$595.96

19. The *Order* did not use any cost data to establish these rates, but instead developed them by applying ratios to the rates for basic 2-wire loops that it adopts. The *Order* did this because it adopted AT&T's Modified Synthesis Model ("MSM") for developing costs for basic 2-wire loops. The MSM, however, is replete with flaws. First, it is based on the model the Commission adopted for determining Universal Service

costs, which the Commission, the D.C. Circuit, and many states have rejected for use in setting state-specific UNE rates. Furthermore, the MSM is not capable of developing costs for *any* of the other unbundled loop products Verizon is required to make available. As a result, the *Order* concluded it had no choice but to use "out-of-model computations" to determine other loop rates. This was incorrect. The *Order* could have used Verizon VA's models that are capable of calculating both DS1 and DS3 costs. The *Order* concluded that these models were consistent with forward-looking pricing principles and, in fact, selected the same Verizon model that calculates DS3 rates as the appropriate model for calculating interoffice transport facility (both dedicated and common) costs.

20. Using ratios to set DS1 and DS3 rates does not result in cost-based rates because there is no logical or consistent relationship between the costs of basic 2-wire loops and high capacity loops. Basic 2-wire loops are provided to residential and business customers at virtually every point in the network, and are provided over facilities with large amounts of copper cable, particularly in the distribution portion of the loop. DS1 loops, in contrast, are usually provided to business customers located in business districts in urban areas, where the loops tend to be located in buildings served directly by fiber-fed digital loop carrier ("DLC") systems. These loops have a much higher proportion of electronics and fiber than 2-wire loops. But the costs of DS1 loops do not *always* reflect that high proportion of DLC costs: in suburban and rural areas, for example, there is less demand for DS1 services, and DS1 loops tend to be provided using at least some copper distribution facilities. In such cases, DS1 loops use twice the copper capacity of a two-wire basic loop, and in these areas, the ratio of costs between DS1s and 2-wire loops will be significantly lower than the ratio in urban areas.

21. The relationship between 2-wire loops and *DS3* loops is even less consistent. DS3 loops are provided using the same type of high-capacity fiber optic systems used in the interoffice transport network and they cannot be provided over the copper facilities or digital loop carrier systems used to provide basic 2-wire loops and many DS1 services. Further, DS3 loops are provided almost exclusively to large businesses with large volumes of voice or data traffic. These customer locations tend not to be distributed throughout Verizon VA's service area in the same way as customers of basic 2-wire loops (or even DS1 loops). As a result, the costs of a DS3 loop provided in Virginia would not vary in a manner that bears any relevance to average two-wire loop costs. Accordingly, there is no basis to believe that there is *any* predictable relationship among the cost of providing basic 2-wire and DS3 loops. While it is, of course, possible as a matter of arithmetic to calculate a ratio between rates for 2-wire loops and for DS1 and DS3 loops, that exercise produces wildly varying results from state to state and region to region, demonstrating that there is no real cost relationship. Attachment 3 shows ratios of DS1 to basic 2-wire loop rates, and DS3 to DS1 rates in Maryland, Massachusetts, New Jersey, New York, and Pennsylvania. This shows, for example, that in Maryland the ratio of DS1 to basic 2-wire loop rates ranges from a low of 4.1 in rate group B1, to a high of 8.1 in rate group A2; in New York, the ratio ranges from 8.3 in density zone 2 to 10.8 in density zone 1a. As another example, the ratios of DS3 to DS1 loop rates range from 10.8 in Maryland and 8.3 in New York to 5.9 in Pennsylvania. This would produce swings in DS3 rates of several hundred dollars. For example, using a statewide average DS1 rate of approximately $100 (such as in New York) with current

DS3 to DS1 ratios in these five states would produce DS3 rates ranging from $590 to $1080.

22. Effects of Rate Reductions. At the time Verizon filed it application to provide in-region interLATA services in Virginia, it faced substantial competition from competitors using their own facilities – either wholly or using unbundled loops in conjunction with the competitor's own switch. Indeed, there was "proportionately more facilities-based competition in Virginia than in any state that has been granted section 271 authority, at the time those applications were filed." *See, e.g., Virginia 271 Order* ¶ 3 (citing Verizon VA Application at 89, Attach. A, Ex. 3)). The reductions in the switching rate that Verizon was required to make as part of the 271 application process changed this focus dramatically, and competitors since then have focused heavily on entry through the unbundled network element platform. For example, just before the October 2002 rate reductions, CLECs in Verizon VA service areas were serving approximately 49,000 lines using UNE-P. By September 2003, that number had increased to more than 250,000. The average number of lines that competitors are adding monthly using UNE-P has grown from 4,000 in the ten months before the rate reduction to more than 18,000 in the ten months after the rate reduction – an increase of more than 350 percent. And the growth rate has continued to increase: competitors are now adding approximately 30,000 new lines per month using UNE-P. *See* Attachment 4.

23. This increase in the use of UNE-P has come at the direct expense of facilities-based competition. For example, while competitors were adding nearly 16,000 lines per month served in whole or in part over their own facilities in the ten months prior

to the October 2002 rate reduction, they have added an average of fewer than 8,000 such lines per month in the ten months after the rate reductions.

24. In particular, there has been a steep decline in the number of lines that CLECs are serving using their own switches together with unbundled loops. Since the October 2002 rate reduction, there has been an absolute decrease (not just a slowing in the growth rate) of more than 18,000 in the number of lines served by competitors using their own switches together with unbundled loops. In the ten months prior to the rate reduction, competitors were *adding* more than 1,500 lines per month using their own switches together with unbundled loops; in the ten months after the rate reduction, competitors have been *shedding* an average of more than 1,800 such lines each month. The total number of lines that competitors are now serving in Virginia using unbundled loops and their own switches is actually *below* the comparable number as of year-end 2001.

25. The shift in focus from facilities-based competition to use of the UNE-P that I describe above has already occurred following the reductions in the unbundled switching rate (and, therefore, the rate for the UNE platform) that Verizon implemented in October 2002 in connection with its application to provide in-region interLATA service in Virginia. The rate reductions required by the *Order* (which, as noted above, will be another reduction in the UNE-P rates that is 150% as much as the reduction previously imposed to meet the Commission's benchmarking standard) will significantly accelerate this trend.

26. <u>Verizon and the public will suffer immediate and irreparable harm if the *Order* is allowed to become effective</u>. As I discussed above, the *Order* will significantly

reduce the rate for the UNE-P below the rate reductions already implemented in October 2002. That will increase the incentive for CLECs to use the UNE-P in Virginia, and diminish any remaining incentives to compete by investing in their own or other alternative facilities.

27. This increased use of UNE-P permanently and irreparably harms Verizon and the public interest. As noted above, Verizon is already losing and will continue to lose more than 30,000 lines per month to UNE-P, which translates into enormous financial losses. This is true because the revenue that Verizon receives from a carrier that purchases a UNE-P line is significantly less than Verizon receives from a retail customer (and substantially below what it costs Verizon to provide the UNEs). Verizon estimates that the total annual revenue loss for the loops and UNE-Ps if the *Order's* rates had been in effect in 2003 would be more than **[BEGIN VERIZON PROPRIETARY]** XXXXX XXX **[END VERIZON PROPRIETARY]**. Based on the historical growth trends for orders of UNE loops and UNE-Ps in Virginia, Verizon estimates that these losses will grow to more than **[BEGIN VERIZON PROPRIETARY]** XXXXXXX **[END VERIZON PROPRIETARY]** in 2004, and more than **[BEGIN VERIZON PROPRIETARY]** XXXX **[END VERIZON PROPRIETARY]** in 2005. As I described above, however, growth of UNE-Ps in Virginia has accelerated rapidly, just as it did in New Jersey following grant of 271 relief and substantial rate reductions there; at the growth rate experienced in New Jersey, Verizon VA's annual revenue losses could be more than **[BEGIN VERIZON PROPRIETARY]** XXXX **[END VERIZON PROPRIETARY]** in 2004, and more than **[BEGIN VERIZON PROPRIETARY]** XXXX **[END VERIZON PROPRIETARY]** in 2005.

28. These estimates are consistent with the conclusions of independent financial analysts. For example, a detailed analysis by one analyst estimated that Verizon loses at least 50 percent of its revenue when it converts a line to UNE-P. *See* Anna Maria Kovacs, Commerce Capital Markets, *The Status of 271 and UNE-Platform in the Regional Bells' Territories* (November 8, 2002) at page 10, Exhibit 1 and page 20, Exhibit 6. Other analysts have also recognized that, because UNE-P is merely resale of Verizon's network at sharply reduced prices, Verizon continues to incur the cost of providing service over the line when a customer's line is lost to UNE-P. Thus, despite losing a large portion of revenue when a line is converted to UNE-P, there are few cost savings associated with the loss of a line to UNE-P. *See, e.g.*, M. Crossman, *et al.*, J.P. Morgan Securities Inc., *Industry Update – No Growth Expected for Bells in 2003* at 15 (July 12, 2002) ("While the Bells lose roughly 60% of the revenues when they lose a line to a UNE-P based competitor, we estimate that they retain 95% of the costs."); F.G. Louthan, IV, Raymond James & Associates, *UNE-P: Unlocking the Impact to the RBOCs* at 5 (October 21, 2002) ("the majority of the costs associated with the local telecom business are fixed in nature . . . When the RBOCs lose lines to UNE-P competitors, they are required to maintain the network in its entirety, making it difficult if not impossible to cut out costs related to an equal percentage of lost lines.").

29. In addition, as noted above, the revenue that Verizon receives from a carrier that purchases a UNE-P line is substantially below what it *costs* Verizon to provide the UNEs. I previously submitted evidence showing that Verizon VA's unrecovered historical cost of providing unbundled loops is $29.14 per month, and the monthly cost of providing the UNE-P is $42.26. As noted above, the unbundled monthly

recurring loop rate established in the *Order* ($14.43) is less than one-half of the unrecovered historical cost of the loop. And while we have not yet completed our analysis of the platform rates, we estimate that the revenue Verizon VA will receive for each UNE-P, based on the *Order,* will be only about 40 percent of the unrecovered historical cost of providing the UNE-P. (As noted above, the unbundled non-loop rate will be less than WorldCom's flat-rate switching proposal of $2.94. Using WorldCom's proposed $2.94 plus the $11.89 loop rate established in the *Order* for Density Cell 1 – which includes approximately three-quarters of Verizon VA's access lines – produces a platform rate of $14.83, which is 35 percent of Verizon's unrecovered historical cost.) Verizon estimates that the total annual shortfall based on our unrecovered historical costs for the loops and UNE-Ps if the *Order's* rates had been in effect in 2003 would be more than $82 million. Based on historical growth trends in the volume of loop and UNE-P orders in Virginia, these rates would produce an additional cumulative shortfall of over $287 million by 2005. As I described above, however, growth of UNE-Ps in Virginia has accelerated rapidly, just as it did in New Jersey following grant of 271 relief and substantial rate reductions there; at the growth rate experienced in New Jersey, Verizon VA's additional cumulative shortfall could be more than $320 million by 2005. Moreover, if Verizon VA leased less than half of its lines as UNE-Ps at the rates that will result from the *Order*, Verizon VA's net income in 2002 would have dropped to zero. To make this determination, I took Verizon VA's reported net income for 2002 from ARMIS ($275,509,000); calculated the annual per-UNE-P shortfall between the *Order's* rate and Verizon VA's UNE-P cost; and then divided the net income by that shortfall amount to produce the number of UNE-Ps that would have to be sold before Verizon VA's net income dropped to zero. Verizon VA's net income would clearly be hugely negative if all of its lines were leased as UNE-Ps.

30. The Commission Staff's recent policy paper confirms that even TELRIC-compliant rates do not provide appropriate cost recovery. The paper concludes, "if investment costs are falling over time, and the period between TELRIC price adjustments is shorter than asset lives, then traditional TELRIC pricing will not permit incumbents to recover the cost of their investment."[2] That shortfall is of course exacerbated by the *Order*'s radical interpretation of TELRIC here.

31. Indeed, the rate produced by the *Order* will not even recover Verizon's actual forward-looking costs. Verizon submitted evidence in this proceeding that a correctly-done TELRIC study produced forward-looking loop costs of $22.33, and a forward-looking statewide platform rate of $35.43. While these costs are below Verizon's actual forward-looking costs, they are a far more reasonable representation of actual forward-looking costs than what the *Order* will produce.

32. If the *Order's* rates had been in effect in 2003, Verizon estimates that the annual shortfall based on our proposed actual TELRIC rates would have been more than $54 million. Based on historical growth trends in the volume of loop and UNE-P orders in Virginia, the rates in the *Order* would produce an additional cumulative shortfall

[2] David M. Mandy & William W. Sharkey, *Dynamic Pricing and Investment from Static Proxy Models*, OSP Working Paper at 1 (Sept. 2003); *see also id.* at 1-2 ("Indeed, when investment costs are falling over time and TELRIC price reviews are conducted at intervals shorter than expected asset lives, the firm will earn less than its target rate of return under traditional implementations of TELRIC."); *id.* at 43 ("When investment costs are falling by 11% per year (as is assumed for switching assets in the FCC Synthesis Model), the TELRIC correction factor is approximately *50%*. That is, switching prices should be increased by *50%* from those suggested by Synthesis Model runs." (emphasis added)).

compared to correctly calculated TELRIC costs of over $197 million by 2005. If growth of UNE-Ps in Virginia matches the New Jersey experience, that additional cumulative shortfall would be more than $219 million.

33. The true-up required in the *Order* will not eliminate these harms. Even if the true-up compensates Verizon VA for some of the financial losses it will incur as a result of the *Order,* it cannot return lost customers or lost customer goodwill to Verizon VA. In addition, a true-up cannot undo the devaluation of Verizon VA's investment or the harm to facilities-based competition that will result from the CLEC subsidies created by the *Order*'s rates.

34. The *Order's* requirement to slash rates for high capacity loops (DS1s and DS3s) will also cause immediate, severe, and irreparable financial harm to Verizon. The reduced rates for unbundled high capacity loops, which will result in reduced rates for the combination of unbundled loops and transport known as enhanced extended links, or "EELs," together with the Commission's new rules governing the availability of EELs, will substantially reduce Verizon's special access revenues.

35. The facilities and services that constitute Verizon's special access services (combinations of loops and dedicated transport) are the same facilities that make up EELS (also combinations of loops and dedicated transport). The difference is one of price. Verizon's special access services are offered in a competitive market at competitive rates. The Commission previously has concluded that Verizon's special access services are sufficiently competitive that it has removed more than 90 percent of Verizon's special access services from retail rate regulation altogether, or has allowed them to be provided under negotiated contracts rather than under tariff at regulated rates.

In contrast, EELs prices based on the DS1 and DS3 rates in the *Order* and the transport rates likely to result are approximately *60 percent* below the prices for our competitive special access services.

36. Verizon has analyzed the impact of the *Order's* rates in light of the requirements in the new rules governing EELs. Based on these rates and the Commission's new rules governing EELs, Verizon has estimated the impact of displacing special access at these new rates. Verizon has concluded that the *Order's* price reductions could result in a net revenue loss of nearly $30 million on an annual basis in Virginia alone by 2005.

37. Moreover, these figures do not take into account additional losses due to the provision at the *Order's* extremely low rates of unbundled high capacity loops that will actually be used primarily for local service (whether individually or in combinations). Unbundled high capacity loops are used predominantly to serve large business customers. Competitive carriers who obtain access to these loops at the *Order's* new rates will be able to compete directly with Verizon for those lucrative customers, but with much lower costs. It is difficult to quantify the number of customers Verizon will lose or to value the goodwill that will be lost from this additional requirement.

38. Finally, as is true in the case of UNE-P as well, the losses that result from the price reductions for high capacity loops and EELs will not be accompanied by any material cost savings. Because Verizon must still provide fundamentally the same service using the same network facilities, it still must incur all the costs to provide the service.

39. For all these reasons, Verizon will suffer immediate, irreparable financial harm if the *Order* is allowed to take effect. In addition, the new rates will dramatically enhance the incentives for CLECs to rely on Verizon's network rather than invest in their own or alternative facilities. That will further undermine efforts to encourage facilities-based competition. As a result, the public interest will be harmed as well.

40. This concludes my declaration.

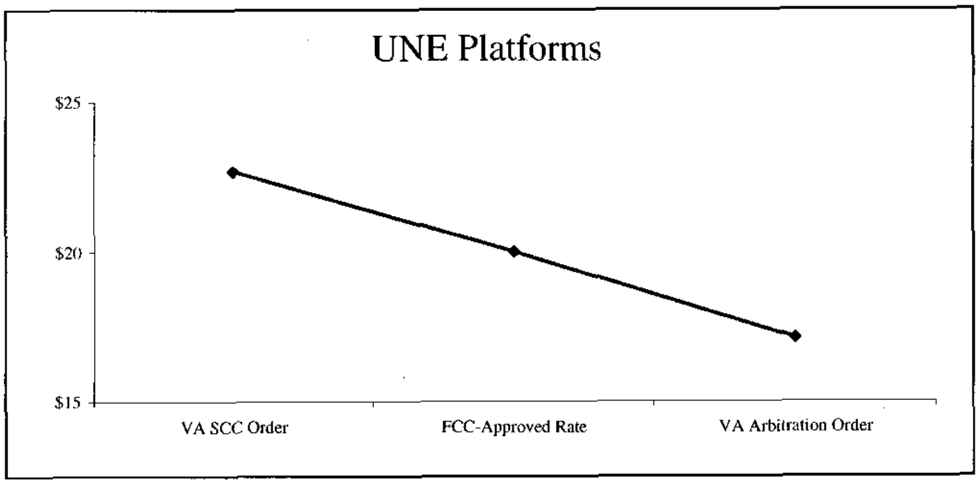
I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

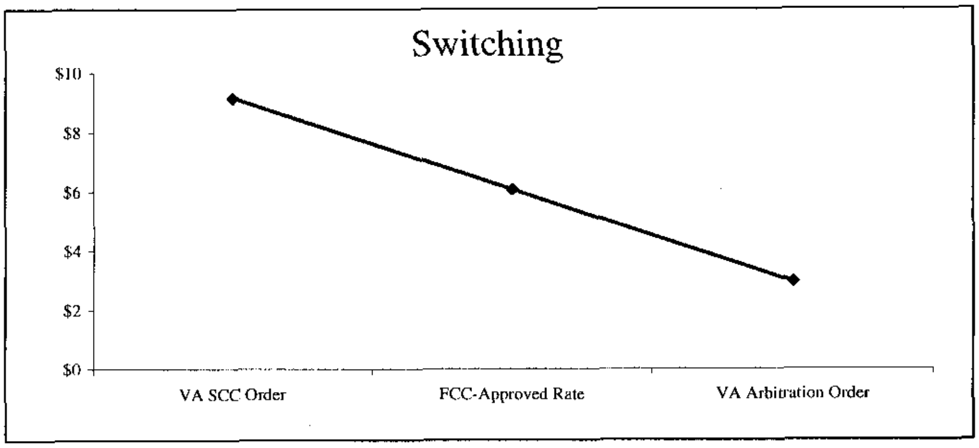
Executed on September 29 2003

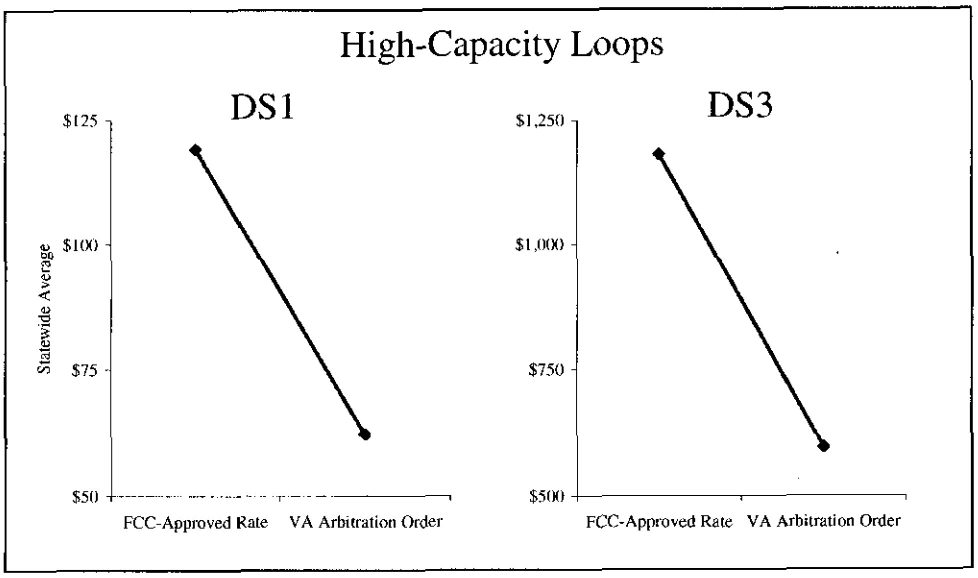
Patrick A. Garzillo

Patrick A. Garzillo

Attachment 1







Bankruptcies With Filing Dates From July 1, 1996 Through September 19, 2003

Sequential Item #	Customer Name	Bankruptcy Filing Date
1	Communications Network Corporation a/k/a Conetco	7/1/1996
2	Heartline Communications	7/23/1997
3	Cherry Communications	10/24/1997
4	American Telecommunications Enterprises	2/9/1998
5	International Telemedia	9/1/1998
6	Equalnet Corporation	9/8/1998
7	Worldwide Direct Inc. a/k/a Conquest Telecommunications and its affiliates	1/19/1999
8	USN	2/18/1999
9	Amnex	5/5/1999
10	Conxus	5/18/1999
11	TeleHub Network Services Corporation	10/27/1999
12	Preferred Carrier	11/18/1999
13	GST Telecom	5/16/2000
14	Net-Tel	9/28/2000
15	Tidalwave Telephone, Inc.	10/16/2000
16	PICUS	11/7/2000
17	ICG Communications	11/14/2000
18	TSR Wireless	12/8/2000
19	Digital Broadband	12/27/2000
20	Pacific Gateway	12/29/2000
21	Darwin Networks, Inc. and affiliates	1/11/2001
22	Northpoint Communications	1/16/2001
23	Vitts	2/7/2001
24	Inet Interactive Network System, Ltd. a/k/a Ins Interactive Network System, Ltd.	2/9/2001
25	North AmericanTelecom	2/23/2001
26	Omniplex Communications Group	2/28/2001
27	Star Tel, Inc.	3/8/2001
28	PT-1 Communications	3/9/2001
29	ConnectSouth Communications, Inc.	3/12/2001
30	Star Telecommunications	3/13/2001
31	Advamtel/Plan B Communications, Inc.	3/16/2001
32	RSL Com USA, RSL Call Prime Com, et al	3/16/2001
33	Jato Communications Corp.	3/21/2001
34	e.Spire Communications, Inc.	3/22/2001
35	Network Two Communications Group d/b/a Weston Information Technologies, Inc. and d/b/a ADP Autonet	3/22/2001
36	ATS Telecommunications Systems, Inc.	3/30/2001
37	Pathnet Telecommunications	4/2/2001
38	Empire One Telecommunications	4/2/2001
39	Winstar	4/18/2001
40	World Access, Inc., WorldxChange and affiliates	4/24/2001
41	PointeCom, Inc. and many affiliates	4/27/2001
42	NewPath Holdings, Inc.	4/27/2001
43	Viatel and many affiliates	5/2/2001
44	Colo.Com	5/8/2001
45	Broadband Office	5/9/2001
46	Onsite Access, Inc., Onsite Access, LLC, Onsite Access Local, LLC	5/16/2001
47	Teligent and 20 affiliates	5/21/2001
48	Weblink Wireless, Inc. d/b/a Pagemart, Inc.and Pagemart Wireless, Inc., Pagemart II, Inc. and Pagemart PCS, Inc.	5/23/2001
49	OAN Services, Inc., a/k/a Operator Assistance Network and EDS OAN Services, Inc.; plus OAN Services of Florida, Inc. And NTelecom Holdings, Inc.	5/25/2001
50	PSINet, Inc. and affiliates	5/31/2001
51	PNI Technologies and its affiliates (including Mercury Communications)	6/8/2001
52	2nd Century Communications, Inc and affiliates 2nd Century Communications Holdings, Inc. and 2nd Century Communications of Virginia, Inc.	6/25/2001
53	Essential.com, Inc.	6/29/2001

Bankruptcies With Filing Dates From July 1, 1996 Through September 19, 2003

Sequential Item #	Customer Name	Bankruptcy Filing Date
54	Metricom, Inc. and affiliates (Metricom DC, L.L.C., Metricom Finance, Inc., Metricom Investments DC, Inc., and Metricom New York , L.L.C.)	7/2/2001
55	Axient Communications, Inc. and affiliate, Axient Leasing, L.L.C.	7/3/2001
56	Star Net Paging, Inc.	7/3/2001
57	Comdisco, Inc. and 50 affiliates (which includes Prism among others)	7/16/2001
58	NetRail, Inc.	7/25/2001
59	Internet Commerce & Communications, Inc, IdealDial Corporation, Application Methods, Inc. et al	7/31/2001
60	Rhythms NetConnections, Inc. a/k/a Accelerated Connections, Inc. and affiliates Rhythms Links, Inc., Rhythms Links, Inc. - Virginia, Rhythms Leasing, Inc. and RCanada, Inc.	8/1/2001
61	DMJ Communications, Inc.	8/1/2001
62	Lineshark Communications, Inc.	8/6/2001
63	Servisense.com, Inc.	8/20/2001
64	Exodus Communications, Inc. and eight affiliates (affiliate names available on request)	9/26/2001
65	Pensat Inc.	10/9/2001
66	Ardent Communications, Inc., d/b/a CAIS Internet, Inc., CGX Communications, Inc. and CAIS Internet, and Ardent, Inc.	10/10/2001
67	Telergy, Inc. and its affiliates	10/26/2001
68	Global Broadband, Inc.	10/31/2001
69	Sure-Tel, Inc.	11/1/2001
70	ParCom Communications	11/3/2001
71	Arch Wireless Communications and its affiliates	11/9/2001
72	Net2000 Communications, Inc.	11/16/2001
73	CoServ LLC d/b/a CoServ Communications,	11/30/2001
74	Enron Corporation and its affiliates	12/2/2001
75	Federal TransTel, Inc.	12/11/2001
76	Startec Global Communications Corp.	12/14/2001
77	Dialpad Communications	12/19/2001
78	Digital Teleport, DTI Holdings, Inc. & Digital Teleport of VA	12/31/2001
79	Home Owners Long Distance, Inc.	1/8/2002
80	Revenue Communications, Inc.	1/15/2002
81	Long Distance Direct, Inc.	1/23/2002
82	Global Crossing and its affiliates	1/28/2002
83	Network Plus Corporation	2/4/2002
84	Verado Holdings, Inc. (a/k/a First World Communications, SpectraNet Communications and/or SpectraNet International) and its affiliates	2/15/2002
85	Logix Communications Corporation and its affiliate, Logix Communications Enterprises, Inc .	2/28/2002
86	Nationwide Communications Inc.	3/5/2002
87	Tek Interactive Group Inc.	3/5/2002
88	In-Touch Software, Inc.	3/11/2002
89	HQ Global Holdings, Inc. and its affiliates	3/13/2002
90	Yipes Communications Group and its wholly-owned subsidiaries of Yipes Transmission, Yipes Transmission VA, Yipes Properties, Inc., Yipes Web Services.	3/21/2002
91	Adelphia Business Solutions Operations Inc. and its affiliates	3/27/2002
92	FNetCorp. a/k/a Franklin Datacom Inc.	4/5/2002
93	Mpower Communications Corp., Mpower Holding Corp., and Mpower Lease Corp.	4/8/2002
94	Lightyear Holding, Inc. (a/k/a Unidial Holding Inc.)	4/10/2002
95	CRG International, Inc. (d/b/a Network One)	4/22/2002
96	Advanced TelCom Group, Inc., Advanced TelCom, Inc., and Shared Communications Services	5/2/2002
97	Metromedia Fiber Network and its affiliates	5/20/2002
98	Teleglobe Inc. and its affiliates	5/28/2002
99	Metrocall, Inc. and its affiliates	6/3/2002
100	Network Access Solutions Corp. (a/k/a NAS ans NASC) and its subsidiary NASOP, Inc.	6/4/2002
101	(11) additional affiliates of Adelphia (naming it Adelphia 2)	6/18/2002
102	Neon Communications Inc. and Neon Optica Inc.	6/25/2002
103	Adelphia Communications Corporation (ACC) and its affiliates (naming it Adelphia 3)	6/25/2002
104	Log On America, Inc.	7/12/2002

Bankruptcies With Filing Dates From July 1, 1996 Through September 19, 2003

Sequential Item #	Customer Name	Bankruptcy Filing Date
105	WorldCom Inc. and its subsidiaries	7/21/2002
106	Telecarrier Services Inc. (a/k/a NSI Communications Services)	7/29/2002
107	Tiagris Corporation	7/30/2002
108	Network Services, LLC	8/1/2002
109	Devon Mobile Communications, LP	8/19/2002
110	Cybertron, Inc. f/k/a Cyber Cities Technologies, Inc. and Cyber City Honolulu and Cyber City Maui	8/21/2002
111	Amerion LLC f/k/a Boss Technologies LLC	9/20/2002
112	Cambrian Communications LLC	9/20/2002
113	CTC Communications Group Inc. and CTC Communications Corp.	10/3/2002
114	Supra Telecommunications d/b/a Supra Telecommunications and Information Systems Inc.	10/23/2002
115	R-Tex Communications Group Inc.	11/12/2002
116	Interplus, Inc. d/b/a Argotech Business Systems	11/22/2002
117	Genuity Inc.	11/27/2002
118	Southwestern Broadband Holdings Inc. f/k/a IP Communications Holdings Inc.	12/6/2002
119	Focal Communications Corporation	12/19/2002
120	Advanced Telecommunications Network, Inc.	1/10/2003
121	IG2 Inc. f/k/a Computer Business Sciences Inc.	1/15/2003
122	BroadbandNow Texas Inc.	2/3/2003
123	DSL Designs Inc.	2/14/2003
124	TalkingNets Inc. and its affiliates	2/19/2003
125	iPCS Wireless Inc.	2/23/2003
126	Superior TeleCom Inc.	3/3/2003
127	Ntelos Inc. f/k/a CFW Communications Company	3/4/2003
128	NOW Communications Inc.	3/4/2003
129	W.G.I. Communications Inc. d/b/a Boomerang Communications Inc.	3/18/2003
130	Big Net Holdings Inc.	3/28/2003
131	Stargate.Net Inc. and its affiliates	4/7/2003
132	Leap Wireless International Inc., Cricket Communications Inc., and their affiliates	4/13/2003
133	Lightband Communications International Inc.	4/22/2003
133	Swiftcomm, Inc.	5/2/2003
134	Duro Comm. Corp. a/k/a Volaris Online	5/8/2003
135	SunTel Communications LLC and its affiliates	5/9/2003
136	Allegiance Telecom Inc. and its affiliates	5/14/2003
137	FASTNET Corporation	6/10/2003
138	Touch America Holdings Inc. and its affiliates	6/19/2003
139	In Touch Communications Inc.	8/1/2003
139	Cypost Corp. d/b/a/Connect NW, d/b/a Internet Arena	8/1/2003
140	RFB Cellular, Inc. d/b/a/ Cellular One of Northeast Michigan, a/k/a Alpine PCS, Inc.	8/5/2003
141	Horizon PCS, Inc., Horizon Personal Comm., & Bright Personal Comm. Services	8/15/2003
142	ProSpeed.Net Inc.	8/19/2003
143	Ciera Network Systems, Inc.	8/28/2003
144	Comm South Companies, Inc.	9/19/2003

Comparison of 2-Wire, DS1, and DS3 Loop Rates

	2-Wire Loop Rates	DS1 Loop Rates	Ratio of DS1 to 2-Wire	DS3 Loop Rates	Ratio of DS3 to DS1 Rates	Source
Massachusetts						
Metro	$ 10.81	$ 54.44	**5.0**			Docket DTE 01-20;
Urban	$ 11.37	$ 73.61	**6.5**			Revised Compliance Filing
Suburban	$ 15.41	$ 83.85	**5.4**			(7/2/2003)
Rural	$ 24.32	$ 130.71	**5.4**			
Statewide	$ 13.93	$ 79.99	**5.7**	$762.68	**9.5**	
Pennsylvania						
Density Cell 1	$ 10.25	$ 117.90	**11.5**			PA Effective Rates
Density Cell 2	$ 11.00	$ 120.62	**11.0**			216 Tariff
Density Cell 3	$ 14.00	$ 146.42	**10.5**			(10/1/2000)
Density Cell 4	$ 16.75	$ 191.17	**11.4**			
Statewide	$ 13.81	$ 155.68	**11.3**	$915.64	**5.9**	
New York						
Density Zone 1a	$ 7.70	$ 82.92	**10.8**			NY - VIP Agreement
Density Zone 1b	$ 11.31	$ 98.18	**8.7**			(Effective March 2002)
Density Zone 2	$ 15.51	$ 129.39	**8.3**			
Statewide	$ 11.49	$ 102.75	**8.9**	$852.79	**8.3**	
Maryland						
Rate Group A1	$ 9.51	$ 75.65	**8.0**			MD PSC - Compliance
Rate Group A2	$ 9.55	$ 76.96	**8.1**			Case No. 8879
Rate Group B1	$ 20.57	$ 99.44	**4.8**			Order 78552 (6/30/03)
Rate Group B2	$ 13.56	$ 89.15	**6.6**			(Retroactive to 12/18/02)
Statewide	$ 11.26	$ 79.54	**7.1**	$860.77	**10.8**	
New Jersey						
Density Cell 1	$ 8.12	$ 68.88	**8.5**			NJ BPU - Compliance
Density Cell 2	$ 9.59	$ 70.99	**7.4**			Docket TO00060356
Density Cell 3	$ 10.92	$ 75.89	**6.9**			(12/17/01)
Statewide	$ 9.52	$ 71.34	**7.5**	$754.83	**10.6**	
Virginia						
Density Cell 1	$ 11.89	$ 51.13	**4.3**			VA FCC Arbitration
Density Cell 2	$ 15.26	$ 65.62	**4.3**			Docket Nos. 00-218 and
Density Cell 3	$ 28.43	$ 122.25	**4.3**			00-251
Statewide	$ 14.43	$ 62.05	**4.3**	$595.96	**9.6**	Order DA 03-2738 ('8/28/03)

Note

(1) DS3 loop rates for Massachusetts, New York, and Virginia assume that customer is located 2 miles from the central office.

Growth of UNE-Platform Lines in Verizon Virginia